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Cost contribution arrangements (CCA) / Cost Sharing

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Concept of CCA

- OECD Guidelines Chapter VIII
- “An arrangement among business enterprises to share the contributions and risks involved in the joint development, production or the obtaining of intangibles, tangible assets or services...”
- Main requirement: The results of the CCA are expected to create benefit for each of the participants.
- Key element: Sharing of contributions in proportion to the expected benefits.

Types of CCA

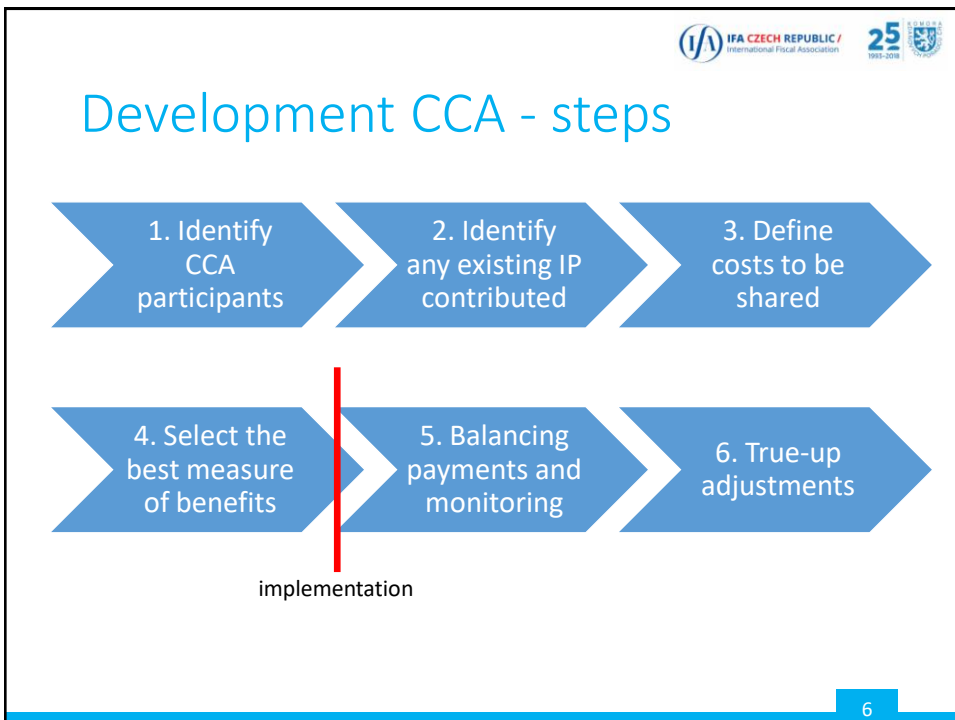
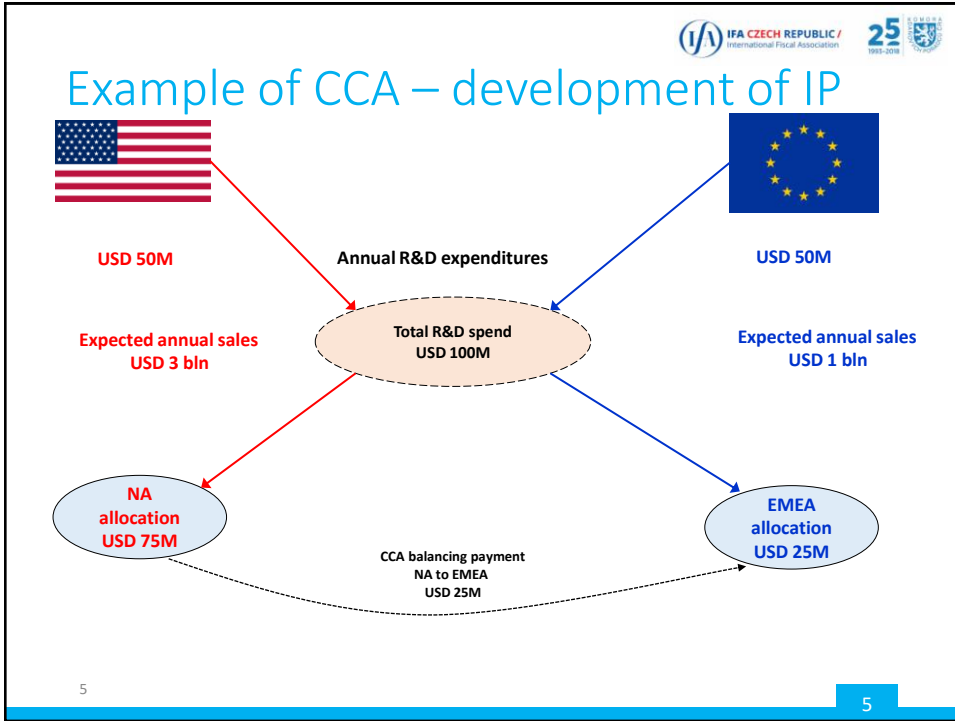
- Development CCA – joint development, production or obtaining of intangible or tangible assets. Expected to create ongoing, future benefits for participants.
- Service CCA – focused on obtaining the services, generally the benefits are more current and certain in nature and less risky.

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Development CCA

- Each participant has an entitlement to the rights in the developed assets. Such rights often take form of separate rights to exploit the intangible in certain geographic location or particular application (e.g. drugs for humans vs animals).
- Legal ownership does not have to be aligned with the economical ownership. In many cases only one CCA participant obtains the formal legal rights but the other participants are granted royalty free licenses.

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Main obstacles observed in practice

1. Identify the CCA participants

- i. participant has to be assigned the rights from the CCA activity and
- ii. has reasonable expectation to benefit from the results of the CCA activity

The mere fact that an entity is involved in the CCA activity does not mean it can be considered a participant of the CCA.

Participant has to exercise control over the risks of CCA and have financial capacity to assume such risks.

- Is a contract R&D service provider a participant of CCA?

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Main obstacles observed in practice

2. Identify any existing IP contributed

- Pre-existing IP contributed to the CCA – valuation methods for the IP.
- May result in one-off initial payment (i.e. platform contribution payment)

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Main obstacles observed in practice

3. Define costs to be shared

- Current contributions – practical approach is to value at costs or cost + mark-up (often R&D costs or marketing costs when developing IP)
- Use of budgeted costs vs. actual costs

Main obstacles observed in practice

4. Select the best measure of benefits

How to measure – depends on the CCA activity / developed IP – sales, profits, units, no. of users, cost savings

Interesting decision is between use of sales vs. profits – what is the better measure? What is the real benefit?

Main obstacles observed in practice

- Uncertainty – in case of IP development, all the benefits are measured now but they will materialize in the future. How to approach it?
- Use of projections
- Reliability of the projections – in practice use of weights or discounting to assign higher value to the closer benefits.
- Need for future adjustments?

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Main obstacles observed in practice

5. Balancing payments

- How to treat balancing payments from accounting, tax , VAT perspective?
- General rule is to follow the treatment as if the contribution was made outside of CCA.
- “any balancing payment should be treated as an addition to the contribution of the payor and as a reduction in the contribution of the recipient”

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Main obstacles observed in practice

6. True-up adjustments

- When to make the TP adjustments?
- What to adjust (costs or also the benefit share)?
- CCA works with multi-year projections of five or even more years. How far back do I have to go?
- Advantage of hindsight of the tax authorities.
- Risk of double taxation.

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CCA take away

- a) All participants must expect to benefit from the CCA
- b) All participants must exercise control over the risks connected with the R&D and have financial capacity to do so.
- c) Contributions of each participant are measured by their arm's length value, practically in case of R&D the value can be measured at costs or costs plus mark-up
- d) Actual costs should be a better measure than budgeted costs, however, significant differences between budgeted and actual costs should be reviewed and agreed by both participants annually
- e) Contributions are split between participants based on expected benefit shares (OECD term) / reasonably anticipated benefit shares (US term) of the participants
- f) Expected benefits can be measured as revenues (sales), units, profits, number of users, cost savings etc.
- g) Expected benefits include mainly future benefits – i.e. projections are used
- h) Balancing payments are made where current contributions in the given year do not correspond to the expected benefit shares
- i) True-up adjustments to be considered

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